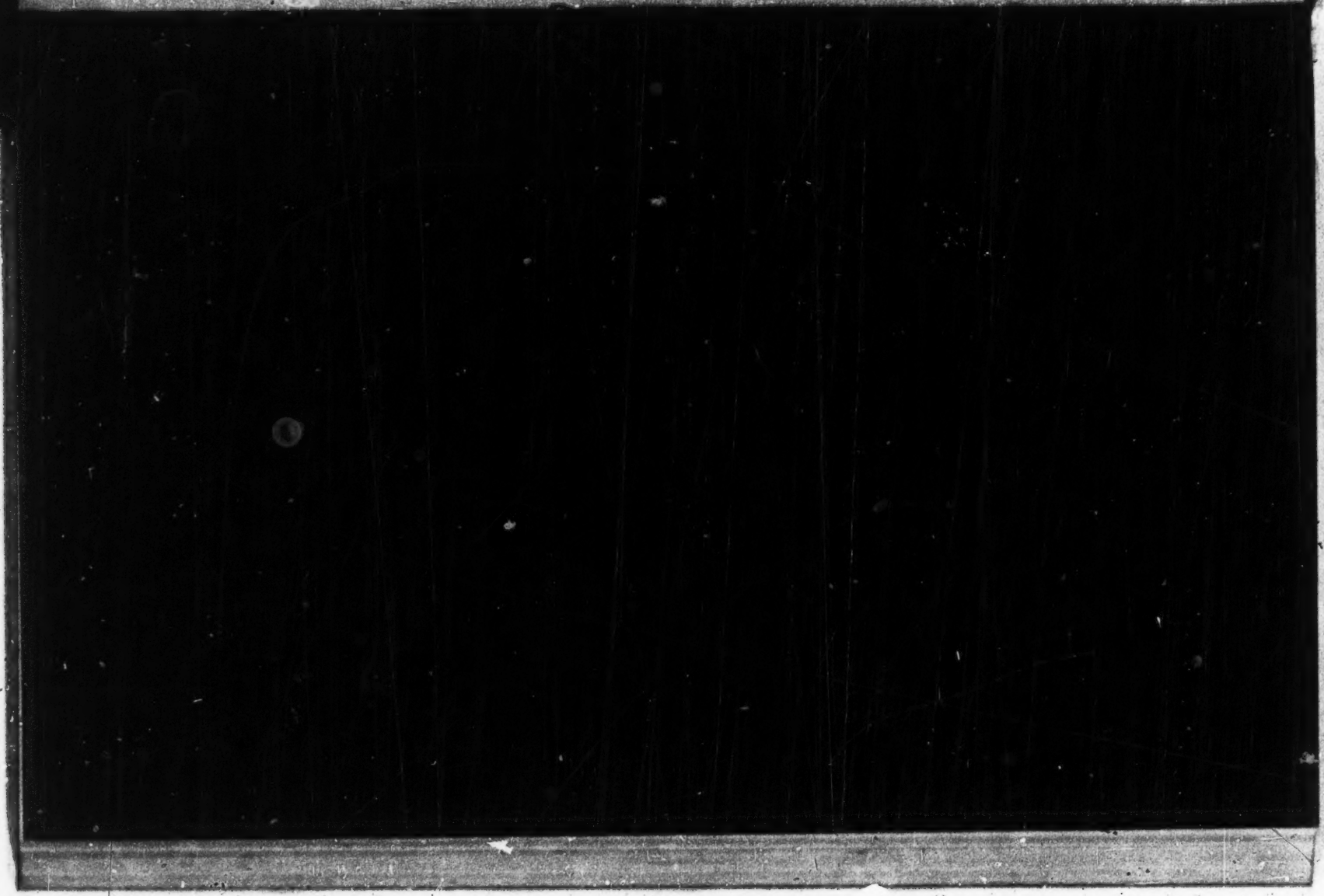

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In the Supreme Court of the United States

OCTOBER TERM, 1938

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHESTER N. WEAVER COMPANY, A CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the decision of the United States Circuit Court of Appeals for the Ninth Circuit entered in the above cause on June 2, 1938 (R. 67).

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 20–38) is reported in 35 B. T. A. 514. The opinion and dissenting opinion in the Circuit Court of Appeals (R. 68–76) are reported in 97 F. (2d) 31.

JURISDICTION

The judgment of the Circuit Court of Apeals was entered on June 2, 1938 (R. 67). The jurisdiction

of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a liquidating dividend is to be treated as a sale or exchange within the meaning of Section 23 (r) (1) of the Revenue Act of 1932, which allows the deduction of losses from sales and exchanges of stocks and bonds which are not capital assets only to the extent of the gains from such sales or exchanges.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 8–11.

STATEMENT

Respondent, a California corporation, on August 9, 1932, purchased 1,000 shares of the preferred stock of Jeff R. Townsend Company, paying therefor $100 per share (R. 22).

Early in 1933 the Townsend Company became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its liquidation and dissolution. On or about September 17, 1933, respondent purchased all the assets of the Townsend Company for $26,280.50. This sum was distributed in liquidation pro rata to the preferred stockholders of the Townsend Company. On September 18, 1933 (less than two years from the date of its purchase), respondent re-

ceived $13,140.25 of the distribution in liquidation, and surrendered its stock certificates for cancellation (R. 22–23).

In its income-tax return for 1933 respondent deducted as a loss the difference between the amount paid for the preferred stock and the amount received in liquidation (R. 23). The Commissioner disallowed the deduction, determining that the loss was sustained from an exchange of stock held less than two years, within the meaning of Section 23 (r) (1); and that respondent had no such gain against which the loss could be applied (R. 13, 23). The Board, five members dissenting, entered an order sustaining the deficiencies (R. 38–39). The Circuit Court of Appeals, Judge Stephens dissenting, reversed the decision of the Board (R. 67).

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that the liquidating dividend was not a sale or exchange within the purview of Section 23 (r) (1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169).

2. In holding that the loss resulting from the liquidation is deductible under the provisions of Sections 22 (d), 115 (c), and 112 of the Revenue Act of 1932.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is in substantial conflict with the decision of the United States

Court of Claims in *White* v. *United States*, 21 F. Supp. 361, now pending on a petition by the taxpayer for writs of certiorari. Nos. 96, 97, October Term, 1938.

The two decisions involve different sections of the revenue laws, but in each the question at issue and the principles governing decision are identical. The *White* case involved the application of Section 101 (b) of the Revenue Act of 1923 (c. 852, 45 Stat. 791) which limits the diminution of income tax to 12½ per cent of capital net loss. The Court of Claims held that section applicable to a liquidating dividend, basing its decision on the fact that Section 101 (c) (2) of the 1928 Act defined a "capital loss" as a "deductible loss resulting from the *sale or exchange* of capital assets" (italics supplied), and that Section 115 (c)[1] provided that liquidating dividends "shall be treated as in full payment *in exchange for* the stock * * *." (Italics supplied.)

The majority of the court below refused to accept that interpretation of Section 115 (c). Section 23 (r) (1) of the 1932 Act, *infra*, p. 9, provides that "Losses from *sales or exchanges* of stocks and bonds * * * which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges * * *." (Italics supplied.) In spite of the fact that Section 115 (c) of the 1932 Act,

[1] Identical with 115 (a) of the 1932 Act.

like Section 115 (c) of the 1928 Act, directed that liquidating dividends be treated as in full payment *in exchange* for the stock, the majority refused to apply Section 23 (r). The opinion states (R. 70) that Section 115 (c) "does not say a liquidating distribution is an 'exchange,' but says it 'shall be treated' as such for the purpose of applying sections 111 and 112." As pointed out in the dissenting opinion, the effect of the decision is to allow the loss as a minus item of gross income under Section 22 (d) (dealing with gross income) and to disregard the provisions of Section 23. The decision imputes to Congress the intention to direct that a liquidating dividend be treated as a sale or exchange in computing the amount of the loss, while it is to be treated otherwise in determining the deductibility of the same loss. The dissenting judge, relying on the *White* case, reached the opposite result.

The conflict between the two decisions is undeniable. Each case turns upon the question whether distributions in liquidation are, under Section 115 (c), subject to provisions governing losses resulting from a sale or exchange of assets. The Government, believing that a conflict exists which should be resolved by this Court, is not opposing the petition for certiorari in the *White* case.[2]

[2] The Government did oppose a petition for a writ of certiorari in *Fairbanks* v. *United States*, No. 65, October Term, 1938. That case is readily distinguishable. There the question involved is whether the gain from the redemption of bonds is a sale or exchange. There is no provision in the Act there involved for so treating such redemption.

2. The court below has erroneously decided an important question of Federal law which has not been, but should be, settled by this Court. Section 115 (c), providing that amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, has been reenacted in the Revenue Acts of 1934 (c. 277, 48 Stat. 680), 1936 (c. 690, 49 Stat. 1648) and 1938 (Pub., No. 554, 75th Cong., 3d Sess.). Hence the problem whether liquidating dividends shall be treated as received upon an exchange within the meaning of sections of the statute other than those mentioned in Section 115 (c) will continue to recur. The question is, in fact, now pending before the court below in connection with the 1934 Act in *Martin General Agency* v. *Commissioner*, on appeal from the Board of Tax Appeals, whose memorandum opinion, not reported, was rendered August 19, 1937.

Furthermore, the court below has cast doubt upon the proper scope of Section 112. If, as the court held, Section 112 (similar throughout the Revenue Acts) allows the *deduction* of a loss where it simply provides that a loss is to be *recognized*, the provisions of Section 23 (r) (1), Section 101 (b), and all other provisions dealing with distributions in liquidation are rendered wholly nugatory. We submit, on the contrary, that the purpose of Section 112 is merely to distinguish between closed transactions wherein the loss is to be recognized, and transactions not closed wherein the loss is not

to be recognized. The amount of the loss is thus determined under Sections 111 and 112; its deductibility is to be determined under Section 23.

CONCLUSION

Wherefore, it is respectfully prayed that this petition for a writ of certiorari be granted.

ROBERT H. JACKSON,
Solicitor General.

AUGUST 1938.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 13. TAX ON CORPORATIONS.

(a) RATE OF TAX.—There shall be levied, collected, and paid for each taxable year, upon the net income of every corporation, a tax of 13¾ per centum of the amount of the net income in excess of the credit against net income provided in section 26.

* * * * *

SEC. 21. NET INCOME.

"Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

SEC. 22. GROSS INCOME.

(a) GENERAL DEFINITION.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(d) DISTRIBUTIONS BY CORPORATIONS.—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

(e) DETERMINATION OF GAIN OR LOSS.—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) LOSSES BY INDIVIDUALS.—Subject to the limitations provided in subsection (r) of this section, in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business;

* * * * *

(f) LOSSES BY CORPORATIONS.—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * *

(r) LIMITATION ON STOCK LOSSES.—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

* * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) COMPUTATION OF GAIN OR LOSS.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis

provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

* * * * *

(c) RECOGNITION OF GAIN OR LOSS.—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) GENERAL RULE.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section. * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(c) DISTRIBUTIONS IN LIQUIDATION.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

Revenue Act of 1924, c. 234, 43 Stat. 253:

DISTRIBUTIONS BY CORPORATIONS

SEC. 201. * * *

(c) Amounts distributed in complete liquidation of a corporation shall be treated

as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 202, but shall be recognized only to the extent provided in section 203. * * *

U. S. GOVERNMENT PRINTING OFFICE: 1938